

Analysis of
Business
Trends Plus
Selected
Financial
Indicators

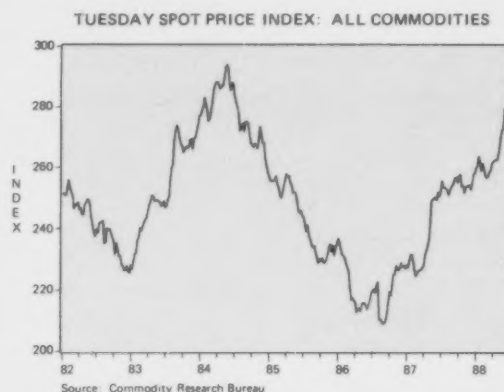
A Summer Lull For Monetary Policy?

The announcement of a smaller-than-anticipated, \$9.9 billion seasonally adjusted U.S. merchandise trade deficit in April provides a positive backdrop for the convening of the Toronto Economic Summit this week. At the meeting, the major industrial countries are expected to express their general satisfaction with prevailing exchange rate levels and the progress achieved so far in reducing global trade imbalances, while concealing any substantive differences regarding such weighty issues as our domestic budget deficit, monetary policy coordination and trade protectionism behind a veil of soothing official pronouncements. Although all this may seem predictable, it does set an appropriate stage for the onset of the summer doldrums in the world's financial and foreign exchange markets.

Closer to home, however, the extent of any summertime lull in the financial markets depends upon whether or not the Federal Reserve is satisfied with the current course of the economy and inflation. If it is, monetary policy initiatives will be put on hold, and few market-jolting surprises will stem from the central bank. If it isn't, the opposite will occur. For a variety of reasons, ranging from a slowing of the pace of business during the second quarter to a less-than-immediate inflation rate threat to the dollar's new-found luster in the foreign exchange markets, it appears a good bet that monetary policy will be held steady in the weeks ahead, thereby providing little in the way of unpleasant excitement for either the financial markets or the growing cottage industry of analysts who look for meaningful implications in every squiggle of the Federal funds rate.

Perhaps the most important reason for expecting a period of monetary policy stability is the emergence of several signs suggesting that the economy's expansion is slowing from its torrid, first quarter pace—a clip which had threatened to quickly produce both capacity constraints and labor market pressures. One indication of this was

contained in the May employment report. Although the number of nonfarm payroll jobs increased by a still healthy 209,000 persons last month, this was far below the nearly 350,000 monthly jobs gain posted in the first quarter.



What's more, a slight dip in the length of the workweek in May and a modest gain in factory jobs could be a forerunner of a slowing of industrial output and personal incomes growth in the months ahead. When all this is combined with the fact that such key indicators as retail sales, construction outlays and the index of leading economic indicators are, at best, only inching higher, it's hard to build a case that the economy is in the midst of an out-and-out boom—surging exports and business capital spending notwithstanding.

Caution On The Inflation Front

The spreading realization that growth is moderating is a decided plus for the financial markets, for slower growth tends to blunt inflation rate pressures before the Fed has to do so with more drastic policy actions. But what is clearly less of a plus is the fact that inflation pressures have already intensified and will probably continue to do so.

For one thing, commodity prices, a usually reliable indicator of future inflation rate trends, are moving sharply higher. With agricultural prices soaring due to the onset of drought in the Midwest, the Commodity Research Bureau's spot price index has spiked to its highest level since July 1984,

Manufacturers
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Department
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and is a whopping 34 percent above its late 1986 lows. To be sure, while the run-up of prices for such agricultural commodities as soybeans and corn could reverse if wetter weather arrives in the farmbelt, the escalation of such industrial commodity prices as copper, tin and zinc is probably more permanent, since it is attributable to rising activity levels and the low-valued dollar (see chart on page 1).

For another, wages are beginning to creep higher, with hourly earnings in May taking their biggest one month jump so far this year. Over the past year, hourly earnings are

up nearly 3½ percent which, although in itself is hardly a threatening surge, is still faster than the 12-month rate of wage gain posted over most of the past two years. On the other hand, too much should not be read into this; the potentially inflationary effects of the upward creep of wages has been more than blunted by productivity gains. In the first quarter, labor costs per unit of output, the key factor in the longer-term inflation outlook, actually fell.

More Good Trade News

With business conditions and the near-term inflation outlook generally supportive of

Short Term Paper Outstanding

(Millions of Dollars)

Time Deposits of \$100,000 or more Weekly Reporting Banks	Latest Week	Change Since Week Ago	Year Ago
Nationwide (6/1/88)	180,485	- 1,830	+ 4,320
New York City (6/8/88)	37,344	- 2	+ 680
Commercial Paper (6/8/88)	414,315	- 66	+ 58,631

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans			
Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Year Ago
Nationwide (6/1/88)	299,507	+ 503	+ 8,357
New York City (6/8/88)	57,261	+ 100	- 4,228
Total Loans and Leases Gross Adjusted			
	Latest Week	Change Since Week Ago	Year Ago
Nationwide (6/1/88)	896,183	+13,570	+43,885
New York City (6/8/88)	174,599	- 6,250	-35,689

Financial Markets

	Friday 6/17/88	Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	6.56%	-	.06 + .76
180-Day Bills†	7.00	+	.05 + .82
Longest Bills†	7.51	+	.10 + .83
Recent Issues:			
81/8S 5/31/90	8.03	+	.10
77/8S 3/31/92	8.45	+	.11
9S 5/15/98	9.03	+	.10
91/8S 5/15/18	9.12	+	.09
Municipals:			
Bond Buyer—20 Bond Index* (6/16/88)	7.73%	-	.05 + .10
Blue List Total (\$ Million)	\$1,560	+	\$225 +\$ 154
30-Day Visible Supply (\$ Million)	\$2,268	+	\$ 32 -\$ 94
Total	\$3,828	+	\$257 +\$ 60
Corporates:			
Moody's Aa Composite (6/16/88)	10.07%	-	.14 + .47
30-Day Visible Supply (\$ Million)	\$4,716	+	\$279 +\$1,313
Stocks:			
Dow-Jones Averages:			
Industrials	2,104.02	+	2.31 -316.83
Transportation	864.10	-	13.29 -162.84
Utilities	180.60	+	1.49 - 24.95
65 Stocks	782.09	-	1.93 -126.43
N.Y.S.E. Composite Index	152.82	-	.07 - 19.75
N.Y.S.E. Avg. Daily Vol. for Week (000's)	201,928	-	2,600 +23,951

*34% Taxable equivalent 11.71%.

† Bond equivalent.

International Rates

	Friday 6/17/88	Week Ago
EURODOLLAR DEPOSIT RATES (bid)		
Overnight	7.38%	7.13%
1 month	7.50	7.56
3 month	7.56	7.63
6 month	7.81	7.75
1 year	8.19	8.13
FOREIGN EXCHANGE SPOT RATES		
New York Opening (6/17/88)	Currency Per U.S. \$	Week Ago
Belgium	36.59	35.93
Canada	1.2143	1.2192
France	5.9025	5.8045
Germany	1.7535	1.7190
Italy	1301.25	1278.25
Japan	125.84	124.90
Mexico	2273.00	2273.00
Netherlands	1.9655	1.9300
South Korea	728.20	728.60
Switzerland	1.4580	1.4354
Taiwan	28.64	28.62
U.K.*	1.7835	1.8190

* U.S. \$ per U.K. pound

MH TRADE-WEIGHTED DOLLAR (6/17/88)	Change Since Week Ago	2/27/85
(Adjusted for Inflation)	+0.8%	-5.8%

monetary policy stability, one of the few "wild cards" left was the dollar's external value. But the potential for any unpleasant surprises on this front receded abruptly with the announcement that the merchandise trade deficit narrowed from a seasonally adjusted \$11.7 billion in March to under \$10 billion in April—a far better result than generally expected. With the trade deficit on the mend, and international interest rate differentials widening in favor of the dollar over the past two months, the question dominating the foreign exchange markets at this time is what are the dollar's upside limits, rather than guessing as to when it will

touch new lows. In this environment, the likelihood of an acceleration of imported inflation is nil, and one large constraint on the flexibility of monetary policy has dissipated.

Nor could the timing of all this have been better. For with the Toronto Summit now underway, the President can bid farewell to his colleagues on a positive note, informing them that the prognosis is good for continued, albeit slower growth, restrained, although gradually rising inflation, a stable dollar and a steady monetary policy—at least for now.

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending 6/15/88	\$ Change Since	
		Week Ago	Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies			
Owned Outright & RPs	232.199	— .037	+17.039
Loans to Depository Inst.	3.651	+ .373	+ 3.000
Float	.381	— .482	— .440
Total Reserve Bank Credit	250.662	— .374	+18.896
Treasury Deposits with			
Federal Reserve Banks	3.110	+ .428	— .769
Currency in Circulation	233.640	+ .073	+18.876
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	227.312	— 1.047	+47.466
Member Bank Reserves:	6/15/88		
Total Reserves Held	61.051	+ 2.253	+ 3.095
Excess (Deficiency)	.686	— .466	— .118
Net Free Reserves	.207	— .363	— .216
		% Change Since	
		3 Months Ago*	Year Ago
Monetary Aggregates †			
M1 (6/6/88)	773.5	+ 6.5	+ 3.3
M2 (6/6/88)	3,018.1	+ 7.8	+ 5.6
M3 (6/6/88)	3,795.2	+ 6.7	+ 6.0
Domestic Nonfinancial Debt (4th Q'87)	8,361.5	+ 10.2	+ 10.0

† Seasonally adjusted.

* Seasonally adjusted annual rate.
‡ Four-week moving average.

New York Money Market

Offering Rates 6/17/88	3 Months	6 Months	1 Year
‡ U.S. Treasury Bills	6.35%	6.64%	6.99%
* Federal Agencies	7.20	7.35	7.45
* Municipal Notes—High Grade (34% Taxable Equivalent)	7.27	7.58	7.88
Negotiable Time CDs			
Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	7.45	7.65	8.00
‡ Finance Company Paper—Prime		‡* Bankers' Acceptances	
5- 14 days	7.35%	Jul.	7.30%
15- 29 days	7.30	Aug.	7.30
30- 59 days	7.35	Sep.	7.30
60- 89 days	7.38	Oct.	7.35
90-179 days	7.38	Nov.	7.35
180-239 days	7.25	Dec.	7.35
240-270 days	7.25		
‡ Industrial Paper—Prime		† Federal Funds	
30- 89 days	7.38%	Effective Rate	7.55%
90-120 days	7.42		
‡ Discount basis.	* Subject to availability.	† Estimated.	

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	1st Q'88	\$ 4,669	\$ 4,607	\$ 4,378
Gross National Product (1982 Dollars)*	1st Q'88	\$ 3,918	\$ 3,881	\$ 3,772
Percent Change, Annual Rate	1st Q'88	3.9	4.8	4.4
Change in Consumer Prices*	Apr '88	4.8%	6.0%	4.8%
Change in MH Cost of Living Index	Apr '88	9.6%	8.4%	7.2%
Change in Producer Prices*	May '88n	6.0%	4.8%	2.4%
Civilian Employment (Thousands of Persons) †	May '88	114,195	114,713	112,334
Unemployment as % of Civilian Labor Force †	May '88	5.6%	5.4%	6.3%
Personal Income*	Apr '88	\$ 3,944	\$ 3,939	\$ 3,702
Leading Indicators Composite Index (1967=100) †	Apr '88	192.2	191.9	187.6
Industrial Production Index (1977=100) †	May '88n	136.0	135.5r	128.2
Net Change in Consumer Installment Credit †	Apr '88n	\$ 3.65	\$ 5.19r	\$ 4.62
U.S. Merchandise Trade Balance †	Apr '88n	—\$ 9.89	—\$ 11.70r	—\$ 13.24
Plant and Equipment Expenditures*	3rd Q'88n	\$438.22(a)	\$429.01(a)	\$393.13
Private Housing Starts (Thousands of Units)*	May '88n	1,384	1,576r	1,599
New Construction Expenditures*	Apr '88	\$ 401.8	\$ 401.2	\$ 396.2
Total Business Inventories †	Apr '88	\$ 723.7	\$ 720.1r	\$ 670.9r
Total Business Sales †	Apr '88n	\$ 478.8	\$ 479.7r	\$ 445.1r

*Seasonally adjusted annual rate.

†Seasonally adjusted.

n-Newly reported figure.

r-Revised.

a-Anticipated.



Innovative

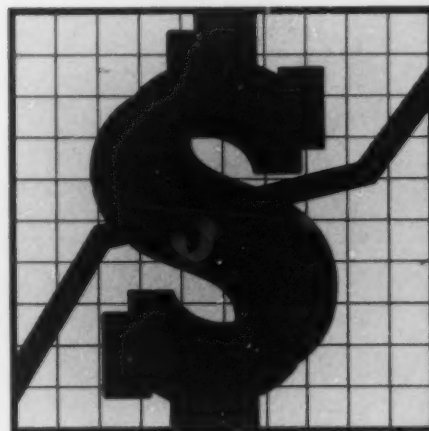
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